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Michael Doolan, Karina Doorley, Mark Regan,
Barra Roantree

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DISTRIBUTIONAL IMPACT OF TAX AND WELFARE POLICIES: BUDGET 2023

Michael Doolan, Karina Doorley, Mark Regan, Barra Roantree[1]

ABSTRACT

Budget 2023 was focused on providing relief to households experiencing reduced purchasing power due to rapid inflation, which is predicted to persist into 2023. In this Special Article we analyse the distributional impact of these reforms. Budget 2023 was unusual as many reforms were one-off measures specifically addressed at combatting cost of living pressures. Compared to a price-indexed 2022 baseline, Budget 2023 left households across the income distribution better off, with the lowest 10 per cent of households experiencing the largest gain; an increase of 1.4 per cent of disposable income. These income gains are driven by one-off measures, with the majority of permanent tax-benefit parameters either being frozen or increased below forecast inflation. Once inflation stabilises – and the need for further one-off measures diminishes – policymakers may wish to consider the adequacy of welfare payments in providing an appropriate standard of living at current market prices.

1. INTRODUCTION

Budget 2023 was announced amidst increasing policy concern about the rising cost of living, as evident in the Budget being brought forward by two weeks to late September. Inflationary pressures that had emerged in the wake of the COVID-19 pandemic and associated shock to spending patterns were amplified by the Russian invasion of Ukraine. This led to a rapid rise in energy prices which Barrett et al. (2022) showed resulted in a substantial increase in energy poverty (households spending more than 10 per cent of disposable income on energy services), with Lydon (2022) and Doorley et al. (2022) highlighting the disproportionate impact of the wider inflationary surge on low-income, elderly and rural households (owing to the fact that energy and food products make up a larger share of their overall expenditure). While policymakers had initially responded to these concerns with a range of measures announced in a 'cost of living package' on 10 February 2022,

1 Funding from the ESRI's Tax, Welfare and Pensions Research Programme (supported by the Departments of Public Expenditure and Reform, Employment Affairs and Social Protection, Health, Children and Youth Affairs and Finance) is gratefully acknowledged. We are grateful to the CSO for facilitating access to the Survey of Income and Living Conditions (SILC) Research Microdata File used to construct the database for the SWITCH tax-benefit model and to the Irish Social Science Data Archive for facilitating access to the Household Budget Survey used in the ITSim model.

further increases in inflation – particularly energy inflation – had eroded much of the gains from this, leading policymakers to promise measures directed at the rising cost of living in Budget 2023.[2]

In this Special Article we examine the tax and welfare measures announced in Budget 2023. We begin by outlining and assessing the taxation measures in Section 2, before turning to consider the social welfare measures in Section 3. Section 4 presents our analysis of the distributional impact of these measures using SWITCH – the ESRI tax and benefit microsimulation model – as well as the cumulative impact of tax and welfare reforms announced to date by the coalition Government over the period 2020 to 2023. Section 5 concludes.

2. TAXATION MEASURES

Table 1 lists the main taxation measures announced in Budget 2023 alongside the full-year cost estimated by the Department of Finance. While most income tax credits rose in nominal terms, the proportional increase of around 4 per cent was below both the Department of Finance's forecast rate of inflation (7 per cent) and the Central Bank of Ireland's forecast compensation per employee (5.8 per cent). This amounts to an effective tax increase, as these credits are worth less to taxpayers in real terms, while a greater share of aggregate earnings will be exposed to the top 40 per cent rate of tax (i.e. 'fiscal drag').

[2] See, for example, https://www.irishtimes.com/ireland/2022/09/08/government-renews-commitment-to-budget-cost-of-living-measures-ahead-of-expected-interest-rate-rise/.

TABLE 1 MAIN BUDGET 2023 TAXATION MEASURES AND ESTIMATED COST

	Cost, € million
Income Tax	
€75 increase to tax credits and rise in Standard Rate Cut-Off	1,226
Rent Tax Credit	200
Universal Social Charge	
USC second band increase from €21,295 to €22,920	77
Housing	
Help-to-Buy extension to 31 Dec 2024	83
Extension of Living City Initiative	0.5
Pre-Letting Expenses	2
Vacant Home Tax	-3
Defective Concrete Products Levy[3]	-80
Carbon Tax	
+€7.50 per tonne of carbon	-151
Excise Duties	
+€0.50 on a packet of 20 cigarettes	-54
Small Cider Producers Excise Relief Scheme	1
Special Exemption Order excise fee reduction	2
VAT	
Zero VAT on newspapers and digital editions	32.5
Zero VAT on defibrillators	0.4
Zero VAT on non-oral Hormone Replacement Therapy	0.8
Zero VAT on non-oral Nicotine Replacement Therapy	0.8
Misc.	
Flat rate compensation percentage for farmers reduced from 5.5% to 5%	-38
Bank Levy extended to the end of 2023	-87
NORA levy reduced to zero	*
One-off cost-of-living measures	
Extension of excise reduction to end of Feb 2023	117
Extension of 9% VAT rate for gas and electricity to the end of Feb 2023	45
Extension of 9% VAT for the hospitality sector to end of Feb 2023	*
20% reduction in public transport extended to end of Dec 2023	194

Source: Budget 2023 Expenditure Report and Budget 2023 Draft Budgetary Plan.
Notes: Costs are in millions of euro per annum and are full year costs for 2023. One-off cost-of-living measures are estimated costs up to a pre-announced end date. Some small schemes are excluded. * indicates no costing was available.

Similarly, the freeze to most Pay Related Social Insurance (PRSI) and Universal Social Charge (USC) thresholds in nominal terms amounts to an effective tax increase for many taxpayers. The main exception to these effective direct tax

[3] Estimated yield from the Defective Concrete Product Levy was reduced to €32 million after the levy was reduced to 5 per cent.

increases was the change made to the income tax standard rate cut-off (SRCO is the point at which the higher income tax rate of 40 per cent begins to apply). This rose by €3,200, meaning a single or individually assessed person will now start paying the 40 per cent rate on earnings above €40,000 (up from €36,800). This represents a proportionate rise of 8.7 per cent, thus outpacing both forecast inflation and earnings growth.

The Government also announced a range of tax measures aimed at addressing issues relating to housing. This includes a new income tax credit for private renters worth €500 per year for those living in unsupported private rental accommodation.[4] This was amended in the Finance Bill to be extended to parents of third-level students who pay their child's rent in Rental Tenancy Board registered leases. The credit will benefit middle income households most as those earning less than circa €18,000 per annum will not have sufficient tax liabilities to benefit from the credit. All renters above this income level will experience a reduction in their income tax liabilities of €500 per year, which will somewhat mitigate the decline in housing affordability for middle income renters shown by Roantree et al. (2022).

The Minister for Finance also announced two new housing related taxes. The first of these is a new Vacant Home Tax which imposes a triple rate of Local Property Tax (LPT) on certain vacant properties. The tax is a welcome supply-side measure of the kind recommended by Morley et al. (2015), Morgenroth (2016), and the Commission on Taxation and Welfare (2022). However, given the low predicted yield (€3 million), the small number of properties affected (less than 9,000),[5] and the relatively low main rate of LPT (0.1029 per cent), the new tax is unlikely to have a material impact on housing supply. This contrasts with the second of the new housing related taxes, a new levy on certain concrete products at the point of first supply to part-fund the (Mica) Defective Concrete Blocks Redress Scheme. Given robust (inelastic) demand for housing and evidence of elastic supply with respect to both prices and costs (Lyons and Günnewig-Mönert, 2022), the economic burden of this new levy is likely to fall on the residents of newly built homes rather than on industry, exacerbating issues of affordability that have been highlighted by Roantree et al. (2022), Doval Tedin and Faubert (2020), and Corrigan et al. (2019) amongst others.

4 The Finance Bill 2022 noted that those receiving supported rent from a housing authority, social housing support, a social welfare source or residing in a cost rental accommodation as per the Affordable Housing Act 2021 would not be eligible to avail of the credit.

5 See https://www.oireachtas.ie/en/debates/question/2022-10-18/278/.

Elsewhere, although the pre-announced increase of €7.50 per tonne of carbon via the carbon tax was implemented on petrol and diesel, the 2 cent per litre levy on diesel and petrol – the NORA levy – was reduced to zero to directly offset the carbon tax at petrol and diesel prices. Other indirect tax measures announced include the zero-rating of VAT on newspapers and digital editions, defibrillators, hormone replacement therapy and nicotine replacement therapy. Some cost-of-living measures introduced during 2022 were also extended for a portion or all of 2023. Reductions in VAT from 13.5 to 9.5 per cent for the hospitality sector, gas and electricity were extended until the end of February 2023. The reduction in (non-carbon) excise duties of 20c per litre on petrol and 15c per litre on diesel was also extended until the end of February 2023, while the 20 per cent reduction to public transport will continue for the whole of 2023.

3. SOCIAL WELFARE MEASURES

The Budget also included a number of changes to social welfare parameters alongside a number of temporary measures aimed at cushioning household incomes from supply-side driven inflation. Personal rates of payments for social welfare schemes were increased by €12 per week, with proportionate rises to additional payments for qualifying children and adults. Undifferentiated increases in personal rates of payment have been a recurrent theme across multiple Budgets (see, for example, Roantree et al., 2018; 2021). As there is much variation in the rates of payments across the social welfare system, undifferentiated increases have the effect of changing the connection between levels of payments and adequacy in an ad hoc way that generates uncertainty for, and inequality across, claimants. Increasing rates of payments as a fixed percentage would maintain the relativities within the current system and would – supplemented by a more regular benchmarking exercise – represent a more coherent approach to the setting of welfare payments.

There were also notable reforms to other payments. The Working Family Payment income limits increased by €40 per week and will equate to a €24 increase in weekly payments to those in receipt of the scheme. The income limit and eligibility for the Fuel Allowance also changed quite substantially. For those single and aged under 70, the Fuel Allowance income limit is set as the maximum weekly state contributory pension rate plus €120 per week. As the maximum state contributory pension rate rose by €12 and the additional income buffer rose from €120 to €200 per week, this will expand the recipient base of Fuel Allowance. The Fuel Allowance will be more generous to those aged over 70 from January 2023 onward, with maximum income limits of €500 (a 35 per cent increase) for singles and €1,000 for couples (a 67 per cent increase). However, despite these changes, most permanent changes to the welfare rates were below the forecast rate of inflation for

2023.This will lead to an erosion of purchasing power for those reliant on fixed income sources if one-off measures are not repeated or welfare payments are not significantly increased in Budget 2024.

The welfare package in the Budget was heavily tilted towards one-off welfare and universal payments to mitigate inflation-induced strain on household finances. Three universal energy credits were announced, payable in November 2022, January 2023 and March 2023. This is a significant fiscal outlay, totalling €1.2 billion. A double payment of Child Benefit will also be paid on 1 November 2022. Additionally, a series of one-off lump sums for those in receipt of specific benefits was announced, with payment occurring during November 2022. Those in receipt of Working Family Payment, Disability Allowance, Carer's Support Grant, Blind and Invalidity Pensions receive a €500 lump sum, while those in receipt of the Living Alone and Fuel Allowance receive €200 and €400 respectively. A double payment of most social welfare schemes will also occur in the week commencing 17 October 2022 and has been labelled an 'Autumn bonus'. To help third-level students, there was also a one-off €1,000 reduction to the student contribution for the 2022/2023 academic year.

On the non-cash benefit side, GP Visit Cards are to be made available to all those in households with income less than €46,000 per annum. The roll-out of GP Visit Cards to so many citizens will require negotiation with GPs. There is evidence that this can take time. The announcement of a roll-out of GP visit cards to six- and seven-year-olds was first announced as part of Budget 2020. It was announced again as part of Budget 2022 but has not yet occurred.

The National Childcare Scheme (NCS) saw an increase in the universal subsidy rate from €0.50 per hour to €1.40 per hour. The income limits and rates of payment of the income assessed component of the NCS were not adjusted. A recent survey of 505 parents with children in registered childcare revealed that half of parents were unaware of financial support available through NCS (IPSOS, 2022). This was contrasted to the very high awareness (>90 per cent) of the Early Childhood Care and Education (ECCE) scheme, which offers up to 15 hours of free care per week to pre-school children. Imperfect take-up of welfare schemes is common and there is clearly significant room for increasing awareness of the NCS amongst parents.

TABLE 2 MAIN BUDGET 2023 SOCIAL WELFARE MEASURES AND ESTIMATED COST

	Cost € million
General	
+€12 (under 66) welfare payments, proportionate increase for qualified adults	436.2
+€12 (over 66) welfare payments, proportionate increases qualified for adults	447.3
+€2 for qualified child	30.4
Working Family Payment	
+€40 per week to income thresholds	16.8
Fuel Allowance	
Threshold for >70s increased to €500 per week for singles and €1,000 for couples	53.5
Threshold increase from €120 to €200 above the maximum rate of the State Contributory Pension	9.8
Disregard Disablement Benefit from assessable means	0
Disregard half-rate Carer's Allowance from assessable means	0
Domiciliary Care Allowance	
Increase personal rate by €20.50 per month	14.1
Extend eligibility to parents of children in acute hospital up to six months post-birth	1
Blind Pension and Disability Allowance	
€25 increase in earnings disregard	1
National Childcare Scheme	
Universal subsidy increased from €0.50 per hour to €1.40 per hour	121
Misc.	
€5 increase to top-up payment to Community Employment, TUS and Rural Social Scheme	7.8
+€2,470 to the Farm Assistance income disregard	0.5
Development of a Pilot Food Poverty Programme	0.4
Extend JobPlus scheme for disadvantaged and minority groups	0.1
Free School Books Scheme	42
One-off cost-of-living measures	
3x €200 household energy credits	1,200
Halloween Bonus	316.4
Fuel Allowance €400 lump sum	148.5
Child Benefit Double Payment	170.4
Living Alone Allowance €200 lump sum	46
Working Family Payment €500 lump sum	23
Disability Allowance, Carer's Support Grant, Blind and Invalidity Pension €500 lump sum	175
€1,000 third-level student contribution fee reduction, €1,000 increase to SUSI grant for postgraduate students and one-third decrease in contribution fee for Apprentices	106

Source: Budget 2023 Expenditure Report.
Notes: Costs are in millions of euro per annum and are mostly full year costs for 2023. One-off cost-of-living measures are yields for 2022, except for the three energy credits which will be payable from November 2022, January 2023 and March 2023. Some small schemes are excluded.

4. DISTRIBUTIONAL ANALYSIS

We use SWITCH (the ESRI's tax benefit microsimulation model) and ITSim (an indirect tax microsimulation tool jointly developed by researchers at the ESRI and the Department of Finance) to assess the combined impact of taxation and welfare policy changes on households' incomes. The range of policy reforms modelled is detailed in Appendix 1. SWITCH is linked to data from the 2019 Survey of Income and Living Conditions (SILC), the primary source of information on household incomes collected annually by the CSO. The data are reweighted to be representative of the 2019 population (in terms of demographics, employment, income and social welfare) and uprated to reflect price and income growth between 2019 and the year of analysis. The scale, depth and diversity of this survey allows it to provide an overall picture of the impact of the policy changes on Irish households, which cannot be gained from selected example cases. ITSim estimates the indirect taxes (VAT and excise duties, including carbon taxes) paid by Irish households on the basis of their reported expenditure, collected by the CSO's nationally representative Household Budget Survey (HBS) in 2015-2016.[6]

In a typical year, we estimate the distributional impact of the new Budget and compare this to a counterfactual inflation-indexed system. However, using forecast inflation for 2023 alone in this exercise would fail to account for the very high unexpected inflation rate in 2022. For this reason, we take a three-year perspective and prepare three sets of baseline and reform scenarios that enable us to estimate the change in living standards due to policy changes between 2020 and 2023.

These baseline and reform scenarios investigate the effect of policy changes between (i) 2020 and 2022 (ii) 2022 and 2023 and (iii) 2020 and 2023 on the distribution of income, compared to a scenario of price indexation in each case (Table 3). Given the prevalence of one-off measures announced for 2022 and 2023, each set of scenarios examines the effect of permanent policy changes separately to the effect of one-off measures. None of our three baseline scenarios include any one-off measures. Temporary interventions do not make up part of the permanent policy system and are therefore excluded when constructing a reference point against which current policy changes can be compared.

6 Incomes are uprated to 2023 levels using earnings indices, and expenditures are uprated to 2023 levels using price growth indices.

TABLE 3 SUMMARY OF BASELINE AND REFORM SCENARIOS

	2020 - 2022			2022 - 2023			2020 - 2023		
	Base 1	Reform 1		Base 2	Reform 2		Base 3	Reform 3	
One-off policies included?	No	No	Yes	No	No	Yes	No	No	Yes
Policy	2020	2022	2022	2022	2023	2023	2020	2023	2023
Indexed to	2022	-	-	2023	-	-	2023	-	-
Indexed by (%)	11.1	-	-	7.1	-	-	19	-	-
Data	2019	2019	2019	2019	2019	2019	2019	2019	2019
Uprated to	2022	2022	2022	2023	2023	2023	2023	2023	2023

Source: Authors' analysis.
Notes: Indexation inflates policy parameters to a given year using CPI. Uprating inflates income levels in the underlying data to a given year using a mixture of earnings and price indices. We use 2022 and 2023 inflation forecasts from the Department of Finance provided at the time of Budget 2023 announcement and available in Department of Finance (2022). One-off policy measures refer to schemes introduced in the Cost-of-Living Budget announced in February 2022 (see Doorley et al., 2022) and specific policies announced in Budget 2023 and listed in Table 2.

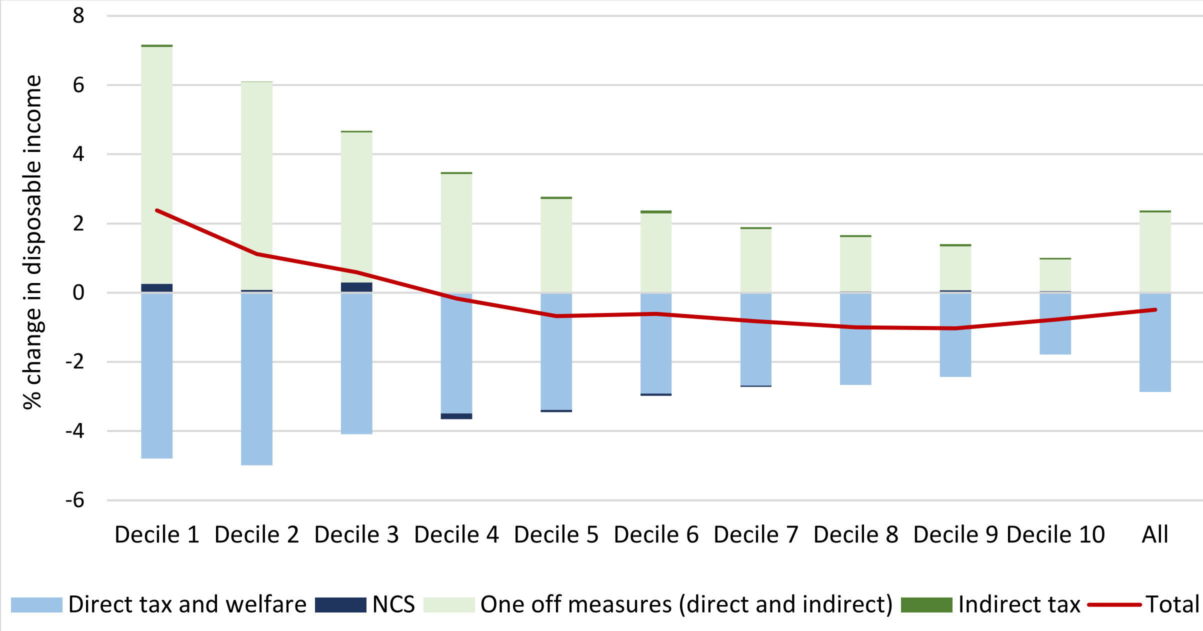
We use SWITCH to calculate households' social welfare entitlements, tax liabilities and net incomes under each system. ITSim calculates households' VAT and excise liabilities, complementing this. The baseline systems are inflation-indexed meaning that the tax credits, bands, thresholds and welfare payments are inflated by the indexation factors included in Table 3, e.g. the 2020 policy parameters increase 11.1 per cent in Base 1, with this factor representing inflation in 2021 and forecast inflation for 2022. Price-indexing provides a benchmark that maintains the purchasing power of households who depend on welfare (at least to the extent that inflation transpires to be no higher than forecast). Wage growth is often cited as a more distributionally neutral benchmark as it ensures equal income growth across the income distribution and keeps average tax rates constant. However, with price growth far outpacing wage growth in 2022, price growth seems a more appropriate benchmark for this exercise.[7]

The effect of policy reform 2020-2022

Figure 1 illustrates the impact of direct tax and welfare and indirect tax policies in 2022 across the distribution of household income, adjusted for family size, with the population divided into ten equally sized groups (deciles) ordered from lowest-to highest income. The reference set of policies is a price-indexed version of the 2020 policy system (disregarding pandemic related policies). The effect of direct tax and welfare measures, indirect tax measures, temporary measures and changes to the National Childcare Scheme are shown separately with the total effect represented by the solid red line.

7 See Callan et al. (2019) for a discussion of indexation options and the associated issues they raise.

FIGURE 1 THE EFFECT OF BUDGETS 2021 AND 2022 ON THE DISTRIBUTION OF INCOME COMPARED TO A PRICE INDEXED 2020 POLICY



Source: Authors' calculations using ITSim linked to the 2015-2016 Household Budget Survey uprated to 2022 prices, and SWITCH run on 2019 Survey of Income and Living Conditions data and uprated to 2022 income levels.
Notes: Deciles are based on equivalised household income, using CSO national equivalence scales.

Permanent tax and welfare reforms between 2020 and 2022 leave households worse off on average, compared to inflation-proofed policies. The pattern of losses is regressive with low income households losing close to 5 per cent of disposable income compared to losses of 2 per cent of disposable income for higher income households. This pattern reflects the fact that permanent increases to welfare payments did not keep pace with inflation over this period. Higher income households benefit more from the tax band and tax credit increases, which came closer to matching inflation. As a result, income losses in the higher deciles are less pronounced.

Indirect tax policy changes and reforms to the National Childcare Scheme have a small effect on household income across all deciles. Indirect tax reforms result in small increases to household disposable income while the effect of the National Childcare Scheme is mixed across the income distribution. Extensions to the Universal Subsidy and increased hours of subsidised childcare drive positive gains in some deciles, while the freezing in cash terms of the income bands for eligibility for the income-assessed component bring about small losses in others.

One-off measures for 2022 provide substantial support, particularly to lower income households. Temporary measures increase household disposable incomes by 6.8 per cent in the lowest income decile, on average. This positive effect continues across higher income households at diminishing magnitudes, with the highest income decile benefitting by 0.9 per cent. On average, across all households, the one-off measures increase household incomes by 2.3 per cent. One-off interventions such as energy credits, fuel excise cuts and VAT cuts on electricity and gas benefit lower income households more in relative terms, due to their lower incomes. Lower income households also benefit to a greater extent from one-off social welfare benefit payments announced as part of Budget 2023, such as the one-off Fuel Allowance payment scheduled for November 2022.

On average, Budget 2021 and Budget 2022 (including one-off measures) reduce average household incomes by 0.5 per cent compared to an inflation-indexed 2020 system. Despite the overall loss, there is a progressive pattern to income changes. Income gains are observed in the lowest three deciles (2.4 per cent in decile one), with small income losses occurring in deciles four, five and six and larger losses identified in deciles seven to ten (1 per cent in decile nine). On average, policy measures, particularly temporary ones, protect low-income households from inflation in a progressive manner and insulate richer households from larger income losses.

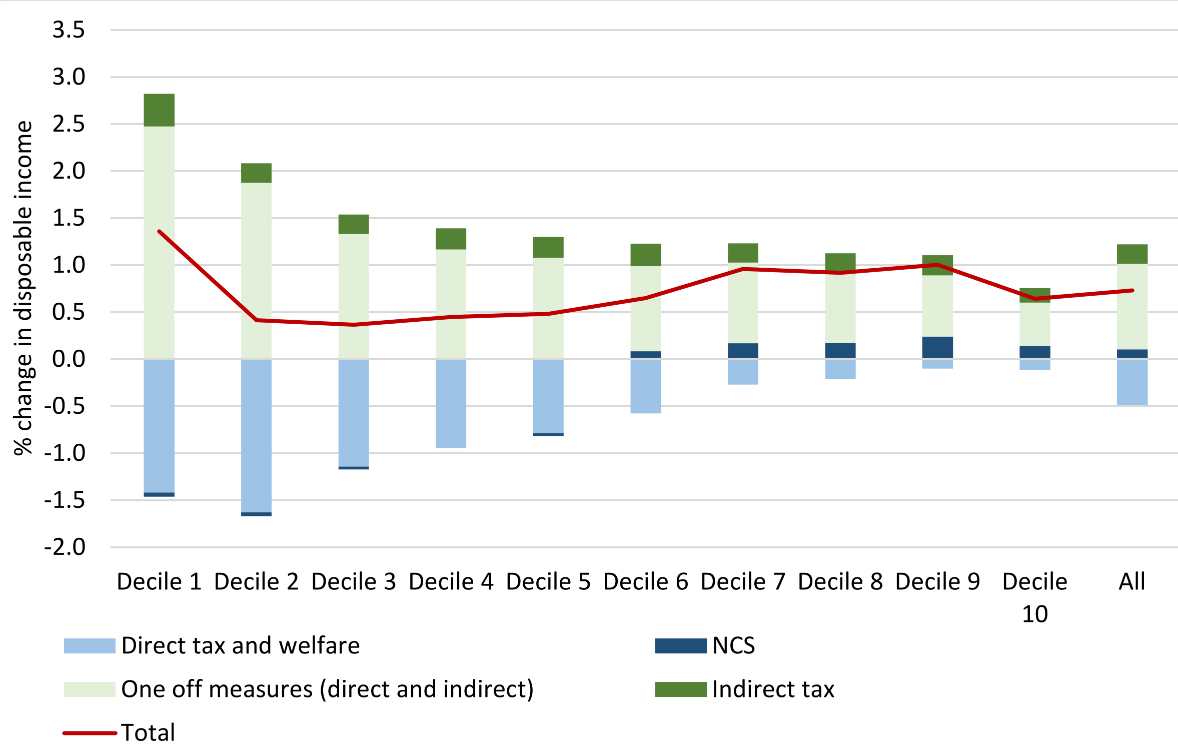
The effect of Budget 2023

Next, we consider the effect of Budget 2023 compared to an inflation-indexed set of 2022 policies. We employ an indexation factor of 7.1 per cent, corresponding to the Department of Finance's 2023 inflation forecast (Department of Finance, 2022). Figure 2 shows the effect of changes to indirect tax, direct tax and welfare, the NCS, and one-off measures announced as part of Budget 2023 that will come into effect in 2023. The baseline is a price-indexed version of the 2022 tax-benefit system temporary measures.

Permanent direct tax and welfare measures do not keep pace with forecast inflation for 2023 in any decile. Lower income households rely more on welfare payments, which were increased below forecast inflation. Higher income households benefit more from the increases to income tax bands and credits, which come closer to matching price increases. Permanent indirect tax policy changes provide an income gain of 0.2 per cent, on average, across deciles. The increase in the rate of subsidy for the universal component of the NCS mainly benefits higher income households whose income is above the limit for the more generous income-assessed component. The freezing of this income limit means that some lower income households lose their entitlement to the income-assessed component of the NCS, resulting in small losses in disposable income in the lower half of the income distribution.

One-off measures increase incomes by 0.9 per cent on average with some variation across the income distribution. Households in the lowest income decile experience average income gains of almost 2.5 per cent while those in the highest income decile experience gains of just under 0.5 per cent. This progressive pattern is largely driven by the fact that one-off universal payments, like the energy credit, have a greater relative impact on low-income households.

FIGURE 2 THE EFFECT OF BUDGET 2023 ON THE DISTRIBUTION OF INCOME COMPARED TO A PRICE INDEXED 2022 POLICY



Source: Authors' calculations using ITSim linked to the 2015-2016 Household Budget Survey uprated to 2023 prices, and SWITCH run on 2019 Survey of Income and Living Conditions data, uprated to 2023 income levels.
Notes: Deciles are based on equivalised household income, using CSO national equivalence scales.

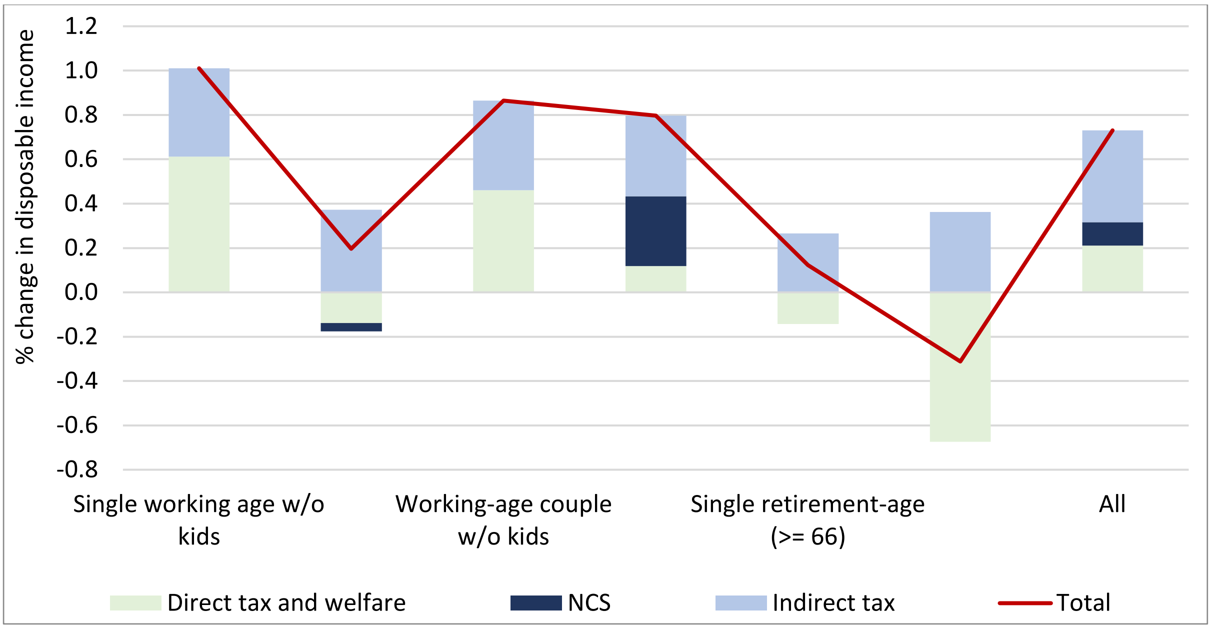
Once again, large one-off measures more than compensate for the set of pre-existing tax-benefit policy changes being outpaced by inflation. Overall, including one-off measures, Budget 2023 leaves households better off on average compared to an inflation-indexed 2022 system. The lowest income decile benefits most (1.4 per cent), with lower gains in the second to sixth decile and tenth decile, and slightly higher gains in deciles seven to nine.

We further examine Budget 2023 by household type, by gender, by earning status and by its effect on income inequality and poverty. All results relate to the Base 2/ Reform 2 with temporary measures scenario, with all one-off policies excluded from the price-indexed 2022 baseline but with one-off policies for 2023 included in the reform.

Figure 3 displays the impact of direct tax and welfare measures and indirect tax policies of Budget 2023 by household type. We show the effect of the NCS separately to other direct tax and welfare to illustrate its effect on the population of families with children. Working-age single and couple households experience income rises of between 0.8 and 1 per cent of household disposable income, compared to an inflation-indexed budget. These household types benefit both from direct and indirect tax and welfare changes. Lone parents and retirement age singles make smaller income gains. Both suffer losses from direct measures, but indirect tax changes counteract these losses for lone parents and partly counteract them for retirement age couples. We observe small losses for lone parents due to the nominal freeze in the rate of the income assessed component of the NCS. The rise in the universal subsidy outweighs this for couples with children who experience a modest gain in disposable income.

Lone parents and retirement age couples benefit relatively less from Budget 2023 than other household types as (i) lone parents are disproportionately affected by the freeze to child benefit and (ii) increases to both the contributory and non-contributory state pensions are further below forecast inflation than increases to working age payments, meaning that retirees fare relatively worse than working-age cohorts. Lone parents and those in retirement are also more likely to be dependent on social welfare compared to other population subgroups, leaving them more exposed to income losses when welfare payments rise less than inflation.

FIGURE 3 THE EFFECT OF BUDGET 2023 BY HOUSEHOLD TYPE COMPARED TO A PRICE INDEXED 2022 POLICY

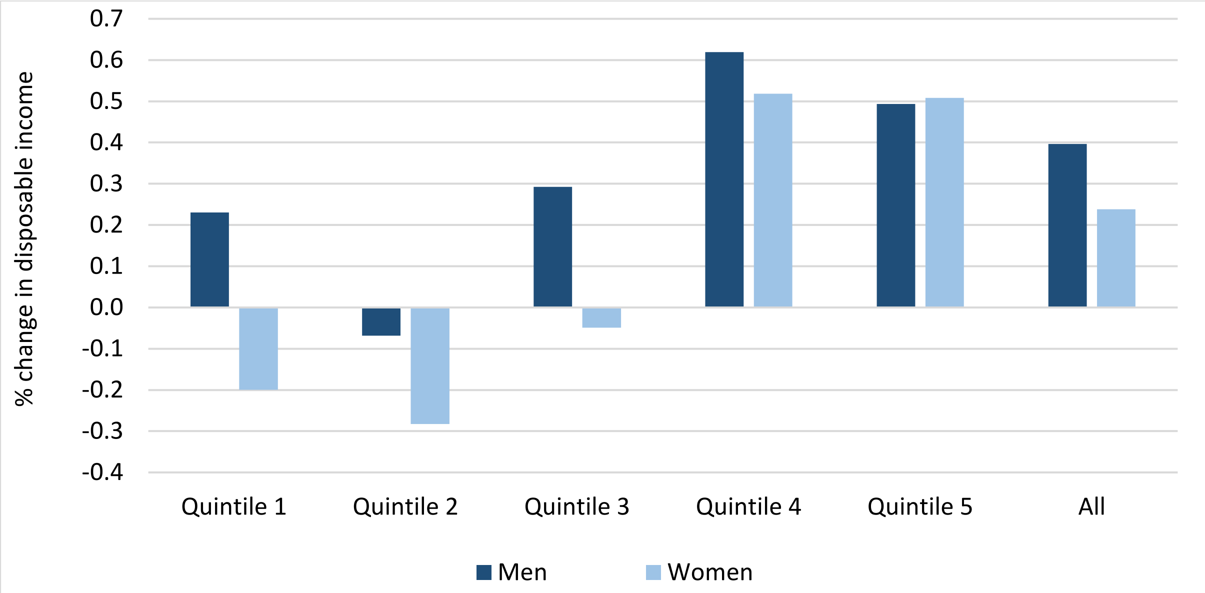


Source: Authors' calculations using ITSim linked to the 2015-2016 Household Budget Survey uprated to 2023 prices, and SWITCH run on 2019 Survey of Income and Living Conditions data, uprated to 2023 income levels.

Figure 4 charts the estimated effects of direct tax and welfare policy changes from Budget 2023 by gender.[8] We assume that income is split evenly between individuals in a couple. Compared to a price-adjusted budget, our analysis suggests that men benefit slightly more than women from Budget 2023, with a disparity of about 0.5 percentage points in decile 1. The gaps are largest in the lower income deciles. This reflects the fact that women are less likely than men to be employed and benefit relatively less from tax cuts and more from welfare increases.

[8] It is not possible to estimate the gender impact of indirect tax changes using ITSim as expenditure data are collected at the household level. The average income changes in this chart are therefore not directly comparable to those in Figures 2, 3 and 5 as indirect tax changes are excluded.

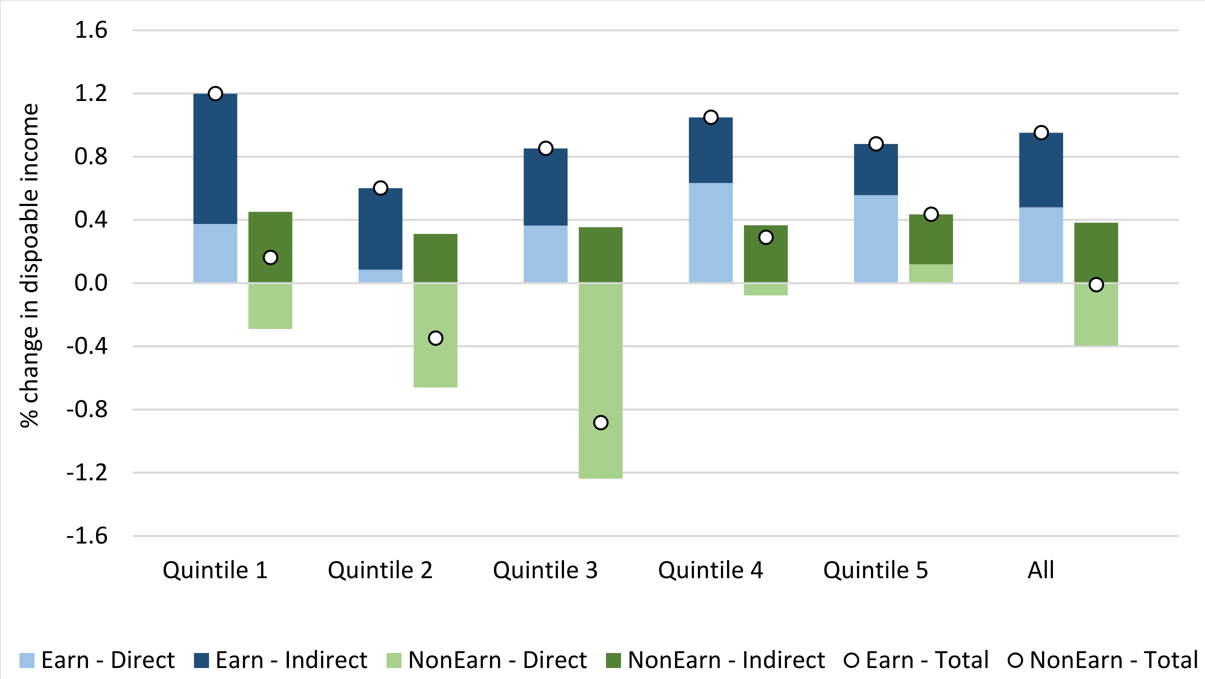
FIGURE 4 THE EFFECT OF BUDGET 2023 (DIRECT TAX AND WELFARE) BY GENDER COMPARED TO A PRICE INDEXED 2022 POLICY



Source: Authors' calculations using SWITCH run on 2019 Survey of Income and Living Conditions data, uprated to 2023 income levels.
Notes: Income is assumed to be fully shared between members of a couple. Quintiles are based on equivalised household income, using CSO national equivalence scales.

Examining the effects of direct tax and welfare and indirect tax changes by earning status, Figure 5 suggests that earners gain relatively more than non-earners from Budget 2023. Higher earners benefit more from direct tax and welfare changes such as above forecast inflation increases to the income tax band. Earners at the lower end of the distribution benefit from the increase to the Working Families Payment income limit. They also gain relatively more from indirect measures such as reduced VAT rates and lower public transport fares. Non-earners in the middle and lower end of the income distribution are left worse off compared to inflation-proofed 2022 policies as a result of below forecast inflation increases to most welfare payments.

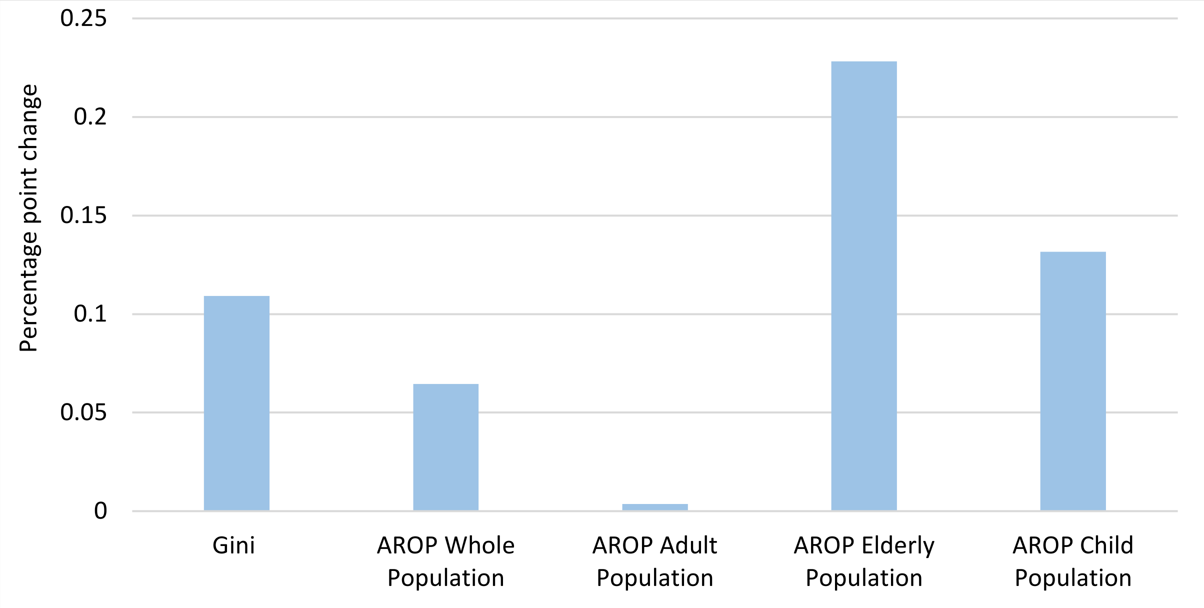
FIGURE 5 THE EFFECT OF BUDGET 2023 BY EARNING STATUS COMPARED TO A PRICE INDEXED 2022 POLICY



Source: Authors' calculations using ITSim linked to the 2015-2016 Household Budget Survey uprated to 2023 prices, and SWITCH run on 2019 Survey of Income and Living Conditions data, uprated to 2023 income levels.
Notes: Quintiles are based on equivalised household income, using CSO national equivalence scales.

Figure 6 shows the estimated effect of Budget 2023 on inequality and 'at risk of poverty' (AROP) measures. Compared to an inflation-indexed system, income inequality, as measured by the Gini index, increases by just over 0.1 percentage point. AROP rates increase across the entire population, but most notably for the elderly and for children. This highlights the fact that these groups are systematically more reliant on social welfare payments, many of which increased below inflation.

FIGURE 6 THE EFFECT OF BUDGET 2023 ON INCOME INEQUALITY AND POVERTY COMPARED TO PRICE-INDEXED 2022 POLICIES



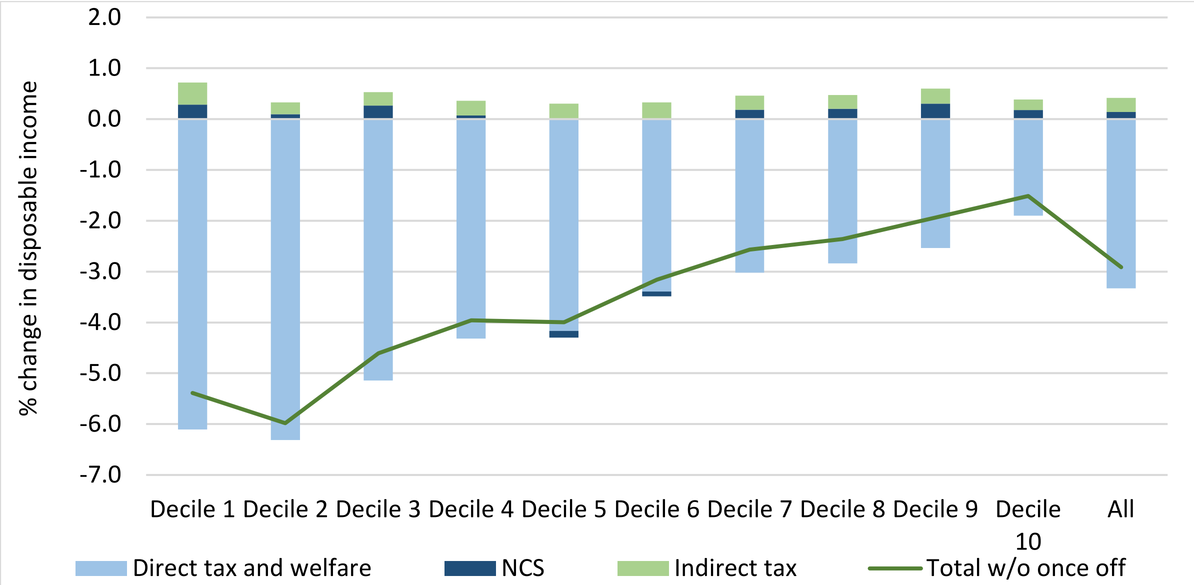
Source: Authors' calculations using SWITCH run on 2019 Survey of Income and Living Conditions data, uprated to 2023 income levels.
Notes: The poverty rate is calculated based on a poverty line equal to 60 per cent of median equivalised disposable income. The CSO equivalence scale is used. Working age defined as aged 18-65 and children as those under age 18.

The effect of permanent policy reform 2020-2023

We next consider how the outlook for households may change if one-off policies are not repeated. To do so, we compare a 2023 policy system without one-off policies to an inflation-indexed 2020 system (Base 3/Reform 3 without temporary measures). Policy parameters in the baseline are indexed by 19 per cent, matching inflation that has occurred and is forecast to occur in 2021, 2022 and 2023.

Figure 7 shows the effects of permanent policy changes in Budget 2023 compared to an inflation-indexed 2020 policy environment. On average, households lose 2.9 per cent of disposable income. Income losses are regressive with lower-income deciles experiencing the greatest erosion in purchasing power. Losses range from 6 per cent in decile 2 to 1.5 per cent in decile 10. There are small average gains across the income distribution resulting from reforms to indirect taxes and the NCS. The average losses, therefore, are overwhelmingly driven by changes to the direct tax and welfare system. This illustrates that permanent policy changes are insufficient to protect the vast majority of households from current and forecast inflation, particularly those with the lowest incomes.

FIGURE 7 DISTRIBUTIONAL ANALYSIS 2020-2023 WITHOUT ONE-OFF MEASURES



Source: Authors' calculations using ITSim linked to the 2015-2016 Household Budget Survey uprated to 2023 prices, and SWITCH run on 2019 Survey of Income and Living Conditions data, uprated to 2023 income levels.

Notes: Deciles are based on equivalised household income, using CSO national equivalence scales.

Comparing Budget 2023 without one-off measures to an inflation-indexed 2020 policy setting conveys the magnitude of the challenge that will be faced in maintaining household living standards when one-off policies lapse. Compared to indexing tax and welfare policies in line with inflation since 2020, Budget 2023 leaves households worse off on average. The permanent budgetary changes – specifically the extension of the standard rate cut-off band – benefit higher income households most, leading to steeper losses for lower income households compared to higher income households.

5. CONCLUSION

Budget 2023 introduced a range of permanent and one-off cost-of-living measures. While these will, on average, insulate households relative to a price-adjusted benchmark, the one-off nature of many of the measures means an erosion of the real purchasing power of structural rates of payments within the social welfare system. There may be a need for further one-off cost-of-living measures in the Winter of 2023 if price rises, particularly energy related, persist next year. Targeted measures will reduce the risk of adding additional demand-side inflationary pressures to the economy.

Once the need for one-off measures to insulate households from inflationary pressures has passed, policymakers may wish to consider benchmarking social welfare payments to reinstate the link between payments and income adequacy.

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APPENDIX 1

TABLE A.1 REFORMS MODELLED IN DISTRIBUTIONAL ANALYSIS

Taxation	Cost, €m	Modelled
Income Tax		
€75 increase to tax credits and rise in Standard Rate Cut-Off	1,226	✓
Rent Tax Credit	200	✓
Universal Social Charge		
USC second band increase from €21,295 to €22,920	77	✓
Housing		
Help-to-Buy extension to 31 Dec 2024	83	
Extension of Living City Initiative	0.5	
Pre-Letting Expenses	2	
Vacant Home Tax	-3	
Defective Concrete Products Levy	-80	
Carbon Tax		
+€7.50 per tonne of carbon	-151	✓
Excise Duties		
+€0.50 on a packet of 20 cigarettes	-54	✓
Small Cider Producers Excise Relief Scheme	1	
Special Exemption Order excise fee reduction	2	
VAT		
Zero VAT on newspapers and digital editions	32.5	✓
Zero VAT on defibrillators	0.4	✓
Zero VAT on non-oral Hormone Replacement Therapy	0.8	
Zero VAT on non-oral Nicotine Replacement Therapy	0.8	
Misc.		
Flat rate compensation percentage for farmers reduced from 5.5% to 5%	-38	
Bank Levy extended to the end of 2023	-87	
NORA levy reduced to zero	*	✓
One-off cost-of-living measures		
Extension of excise reduction to end of Feb 2023	117	✓
Extension of 9% VAT rate for gas and electricity to the end of Feb 2023	45	✓
Extension of 9% VAT for the hospitality sector to end of Feb 2023	*	✓
20% reduction in public transport extended to end of Dec 2023	194	✓
Social Welfare	**Cost, €m**	**Modelled**
General		
+€12 (under 66) welfare payments, proportionate increase for qualified adults	436.2	✓
+€12 (over 66) welfare payments, proportionate increases qualified for adults	447.3	✓
+€2 for qualified child	30.4	✓
Working Family Payment		
+€40 per week to income thresholds	16.8	✓

Contd.

TABLE A.1 CONTD.

Social Welfare	Cost, €m	Modelled
Fuel Allowance		
Threshold for >70s increased to €500 per week for singles and €1,000 for couples	53.5	
Threshold increase from €120 to €200 above the maximum rate of the State Contributory Pension	9.8	✓
Disregard Disablement Benefit from assessable means	0	
Disregard half-rate Carer's Allowance from assessable means	0	
Domiciliary Care Allowance		
Increase personal rate by €20.50 per month	14.1	
Extend eligibility to parents of children in acute hospital up to six months post-birth	1	
Blind Pension and Disability Allowance		
€25 increase in earnings disregard	1	✓
National Childcare Scheme		
Universal subsidy increased from €0.50 per hour to €1.40 per hour	121	✓
Misc.		
€5 increase to top-up payment to Community Employment, TUS and Rural Social Scheme	7.8	
+€2,470 to the Farm Assistance income disregard	0.5	
Development of a Pilot Food Poverty Programme	0.4	
Extend JobsPlus scheme for disadvantaged and minority groups	0.1	
Free School Books Scheme	42	✓
One-off cost-of-living measures		
3x €200 household energy credits	1,200	✓
Halloween Bonus	316.4	✓
Fuel Allowance €400 lump sum	148.5	✓
Child Benefit Double Payment	170.4	✓
Living Alone Allowance €200 lump sum	46	✓
Working Family Payment €500 lump sum	23	✓
Disability Allowance, Carer's Support Grant, Blind & Invalidity Pension €500 lump sum	175	✓
€1,000 third-level student contribution fee reduction, €1,000 increase to SUSI grant for postgraduate students and one-third decrease in contribution fee for Apprentices	106	✓

Source: Budget 2023 Expenditure Report and Budget 2023 Draft Budgetary Plan.